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In the Supreme Court of the United States

OCTOBER TERM, 1968

NEW YORK CREDIT MEN'S ADJUSTMENT BUREAU, INC.,
PETITIONER

v.

UNITED STATES OF AMERICA, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

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In the Supreme Court of the United States

OCTOBER TERM, 1968

No. 384

NEW YORK CREDIT MEN'S ADJUSTMENT BUREAU, INC., PETITIONER

v.

UNITED STATES OF AMERICA, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

In January 1964, Samuel Chapman, Inc., filed a petition for an arrangement under Chapter XI of the Bankruptcy Act. The debtor was permitted to operate its business as a debtor in possession. In the course of its business operations it withheld federal income and F.I.C.A. taxes from wages paid to its employees but failed to deposit in a federal reserve bank, as required by the Internal Revenue Code, either the withheld amounts or the employer's portion of em-

ployment taxes. The debtor also failed to file timely employment tax returns for the second and third quarters of 1964.[1] The debtor was adjudicated a bankrupt in November 1964. (Pet. A4, A14.)

The District Director assessed $2,388.28 of delinquency penalties under Section 6651 of the Code for failure to file timely tax returns and $398.04 of penalties under Section 6656 for failure to make timely deposits. After the adjudication in bankruptcy the District Director filed a proof of claim for payment of various taxes, including these penalties, as administrative expenses of the arrangement.[2] The trustee objected to the portion of the claims that represented penalties. The referee and the district court upheld his objection, but the court of appeals reversed. (Pet. A4-A7.)

The decision of the court of appeals is correct. Legislation effective in November 1967 changed the rules applicable here, so that no general importance attaches to the issue decided below. There is no conflict of decisions or other ground warranting further review by this Court.

1. Since the tax liabilities incurred during the second and third quarters of 1964 resulted from the operation of a business by a debtor in possession during

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[1] The debtor's return for the second quarter was filed in September 1964, and the return for the third quarter was filed in December 1964, each more than a month after their due dates.

[2] The Service's claim for administrative expense taxes also included unpaid income withholding and F.I.C.A. taxes for the third and fourth quarters of 1964 and unpaid F.U.T.A. taxes for 1964.

an arrangement proceeding, Section 960 of the Judicial Code, 28 U.S.C. 960, applies. That statute provides as follows:

> Any officers and agents conducting any business under authority of a United States court shall be subject to all Federal, State and local taxes applicable to such business to the same extent as if it were conducted by an individual or corporation.

This provision makes both trustees in bankruptcy and debtors in possession liable for federal taxes. The tax which Section 960 directs court officers and agents to pay "to the same extent" as ordinary businesses embraces the entire tax imposed by the revenue act and includes penalties that are added to tax, which this Court has recognized to be "the traditional and almost universal method of enforcing prompt payment." *Boteler* v. *Ingels*, 308 U.S. 57, 61; see, also, *Nicholas* v. *United States*, 384 U.S. 678, 692.

A contrary result is not required (see Pet. 7-9) by Section 57j of the Bankruptcy Act, 11 U.S.C. 93, which disallows the payment of penalties out of a bankrupt estate to the United States or to a State or subdivision. As the petitioner observes (Pet. 3), there is no conflict, and this is the first decision on point. Petitioner does not and could not question the liabilities of the debtor for penalties incurred during the arrangement and of the trustee for penalties incurred after adjudication. In *Nicholas* v. *United States*, *supra*, penalties wer sustained against a trustee in bankruptcy for taxes incurred while the debtor was in possession during the Chapter XI arrangement;

the time for filing returns did not occur until after the arrangement had failed and had been superseded by a liquidating bankruptcy. Even though the exact question of the present case was expressly reserved in *Nicholas* (384 U.S. at 693, fns. 27 and 28),[3] the holding of *Nicholas* is inconsistent with any notion that Section 57j is an absolute bar to the imposition of penalties on the basis of events occurring after the arrangement begins.

2. Legislation enacted during the pendancy of these proceedings has eliminated any significant importance this issue may have had in the administration of the bankruptcy or revenue laws. The enactment on November 28, 1967, of P.L. 90-157, 81 Stat. 511, amended Section 378 of the Bankruptcy Act, 11 U.S.C. 778, to require, *inter alia*, in Section 378(c), that administrative claims of the superseded proceedings should be proved and filed in the manner provided in Section 57 of the Bankruptcy Act. The Internal Revenue Service has interpreted this amendment as requiring the application of Section 57j to preclude the allowance of penalties in cases where Chapter XI arrangements become liquidating bankruptcies on and after November 28, 1967.[4] Thus the issue tendered here is unlikely to recur with respect to federal tax penalties. Even if the issue is raised by some State or other

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[3] The court of appeals noted, however (Pet. A7), that part of the penalties claimed in the present case represented a default by the trustee and, accordingly, would come under this Court's rule of *Nicholas*.

[4] The Internal Revenue Service, we are advised, will soon publish this administrative interpretation.

government agency, the decision would necessarily focus on the effect of the 1967 amendments, a factor that would not bear on the result in this case.

Respectfully submitted.

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